7/5/81

Financial Markets

Irving Trust

Irving Trust Company
One Wall Street
New York, NY 10015

Economic Research & Planning Division

Friday
(Noon)

June 26, 1981

The market for bank reserves in the statement week ended last Wednesday can only be described as sloppy, as several corrections to Federal Reserve projections of reserves availability probably required the Fed to arrange "defensive" open market operations. The most vivid instance was the Tuesday reserves-draining operation following Monday's reserves injection. Against the background of a highly volatile Federal funds rate, the financial markets remained nervous, and rates on balance posted only small changes.

Weighing on market sentiment is the spreading recognition that the Fed has not made any overt move to ease the pressure on bank reserves. Such easing as has occurred has been due almost totally to the relatively modest impact on required reserves of the recently sluggish growth of M-1B. That is also true of the current statement week. Though some observers interpreted the Fed's execution of four-day repurchase agreements on Thursday as an aggressive move toward ease, it appears more likely that the intent was to provide the needed reserves at the outset of the statement week, so as to avoid a repetition of last week, when the funds rate was high before the weekend and soft afterwards. Similarly, the three-day RPs today were probably necessary due in part to withdrawals from the four-day RPs.

There is a fair probability that an overt move to make reserves provision more ample will be made at the Federal Open Market Committee's meeting on July 7. Unless the outlook alters radically during the next two weeks, the FOMC will confront a situation in which M-1B is growing at or below its target, while staff projections for future growth of GNP and the money supply will probably have been revised downward. However, a major uncertainty clouding this picture will be the impact of the new spending and tax-cut package in the latter part of the year. Unquestionably, the FOMC ardently wishes to avoid a repetition of the late 1980 surge in money growth, and the fiscal changes currently being enacted by the Congress will have to be carefully weighed with respect to their prospect of causing this to happen. In addition, with the FOMC currently giving more weight to M-2, more pressure on reserves positions (and interest rates) is warranted than would otherwise be the case, since the non-M-1B components of M-2 have zero or minimal reserve requirements and in many cases pay market interest rates.

Interestingly, on Thursday Chairman Volcker floated a proposal that might ease interpretation of M-1B and M-2 by putting reserve requirements on checkable money market mutual fund share balances. The idea would be to encourage individuals to segregate their transaction balances from their savings-oriented balances, thus facilitating measurement of the two. In addition, the proposal would meet some of the complaints made by banking and thrift industry groups, for which transaction balances are subject to reserve requirements. However, while the Administration remains opposed, the proposal has minimal prospects of passage, and so may have been largely a political gesture. Nevertheless, it does call attention to a real problem of interpreting the monetary aggregates.

William C. Melton

Note: The full text of the letter is available to Telerate subscribers on pages 7250-51 on the Monday morning following the Friday date of the letter.

Irving Trust

Market Yields

	6/26/81 Noon	Week Ago	Year Ago
Prime Lending Rate at Irving Trust Company	20.00%	20.00%	12.00
Effective since	6/2/81		
Discount Rate at Federal Reserve Bank	14.00	14.00	11.00
Federal Funds	18.50	21.50	9.38
Repurchase Agreements	15.00	19.50	8.00
U.S. Treasury Issues			
Bills			
3 months	14.75	16.17	7.75
6 months	15.10	15.93	8.08
1 year	14.70	15.38	8.35
Coupons			
2 years	14.46	14.83	8.90
4 years	14.10	14.35	9.22
7 years	13.88	13.80	9.40
10 years	13.64	13.58	9.82
Long Bond	13.09	13.02	9.93
Negotiable Certificates of Deposit-Secondary Market			
1 month	17.45	18.50	8.75
3 months	16.85	17.85	8.75
6 months	16.20	17.00	8.80
1 year	15.75	16.40	NA
Banker's Acceptances			
1 month	17.25	18.65	8.75
3 months	16.85	17.90	8.70
6 months	16.40	17.03	8.80
Eurodollar Deposits			
1 month	18.38	19.00	9.19
2 months	18.00	18.63	9.25
3 months	18.00	18.63	9.44
Commercial Paper - Prime Names			
Directly placed by:			
Finance Companies			
1 week	17.00	18.00	8.25
1 month	16.50	17.00	8.00
3 months	15.00	15.00	7.75
Bank Holding Companies			
1 month	16.75	18.00	8.00
Dealer Placed:			
3 months	16.50	17.13	8.25
New AA Corporate Utility Bond	15.75	15.75	11.50
Tax Exempt			
6 month Project Notes	7.50	7.40	4.50
1 year AAA Bond	8.00	8.00	4.60
5 year AAA Bond	8.75	8.50	5.15
20 year AAA Bond	10.15	10.10	6.90

This information represents prevailing market yields.
It should not be construed as an offering.
All yields are on the offered side of the market.

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